



M e m o r a n d u m

To: Panel Members

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From: Peter McNamee, Executive Director

File: wagememo

Subject: USE OF TIPS AS WAGES

The Employment Training Panel's (ETP) enabling legislation requires that trainees earn at least an ETP required wage (presently ranging from \$11.15 to \$12.16 per hour for retrainees, and \$9.12 to \$10.14 an hour for new hires, depending on county of employment), after completing training and the required employment retention period. Provided that trainees earn at least the State minimum wage (currently \$6.75 an hour), the Panel allows employer paid health benefits, commissions, and tips to supplement trainee wages, in order to meet the ETP minimum requirement. Recently, however, the use of tips to augment a trainee's base wage has been questioned especially in cases where the cost of the training is high, but trainee wages are low (and must be supplemented by tips). There is concern that since tips are not paid by employers, allowing tips in the wage calculation may not be consistent with the Panel's mission to

-wage, high skill jobs."

The following is a summary of the Panel's trainee wage requirements, including a brief history of these requirements; a review of current wage calculations, including the use of tips as wages; a discussion of the issues relevant to the use of tips as wages; and options for potential Panel action.

ETP Wage Requirements

Prior to 1990, there were no statutory ETP minimum wages. In 1990, legislation was enacted requiring ETP to adopt a state-average hourly wage that trainees must earn following training and employment retention. However, these minimums could be waived with evidence of regional or occupational differences to justify a lower wage. As a result, there were long delays in obtaining the final approved wages in cases where the lower minimum wages were requested. This often resulted in significant delays in the contracting process.

Effective January 1, 1994, the legislation was amended. Training for "high-wage, high skill jobs" was emphasized and wage requirements for calculating and applying the minimum wages were simplified by establishing an absolute minimum. Under the current method, the Employment Development Department's (EDD) Labor Market Information Division (LMID) provides both county and state-wide hourly average wage figures, upon which the Panel bases its calculations of minimum wages.

The current Unemployment Insurance (UI) Code Section 10201 (f) stipulates the following, regarding minimum wages required in ETP funded contracts:

“...the employment shall provide earnings¹, upon completion of the employment requirement specified in subdivision (f) of Section 10209, equal to 50 percent, in the case of new hire training, or 60 percent, in the case of retraining, of the State or regional average hourly wage. However, in no case shall the employment result in earnings of less than 45 percent of the state average hourly wage for new hire training and 55 percent of the state average hourly wage for retraining.”

UI Code, Section 10201 (f) allows the Panel to consider the dollar amount of voluntary employer-paid health benefits to supplement a trainee's base wage in order to meet ETP wage requirements. These employer-paid benefits include medical, dental, and vision insurance. In addition, the Panel also allows the use of commissions and tips, as explained below, to supplement trainee wages in order to meet the ETP minimum wage.

The Panel uses these criteria to calculate its minimum trainee wage requirements for projects in each calendar year.

Tips as Wages

The Panel's allowance of tips as wages to meet the minimum requirements can be better understood in the context of how tips and wages are defined in law. Prior to 1986, tips received by employees from persons other than their employer were subject to Disability Insurance (DI) and Personal Income Tax (PIT) withholding, however, not for purposes of Unemployment Insurance. Effective January 1, 1986, UI Code, Section 927.5, was amended, requiring workers to report cash tips to their employers, which were subject to UI, DI, Employment Training Tax (ETT), and PIT withholding. Essentially, tips are now considered wages for the purpose of taxing employers on an employee's earnings.

UI Code, Section 927 defines wages as “all remuneration payable to an employee for personal missions and bonuses, and the reasonable cash value of all remuneration payable to an employee in a medium other than cash.” UI Code section 927 includes with the term “wage,” “all tips which are received while performing services which constitute employment and included in a written statement furnished to the employer pursuant to section 6053(a) of the Internal Revenue Code.” Further, the California Code of Regulations requires workers to report tips to their employers of \$20 or more received in a month. As such, the tips are considered taxable earnings, or wages. In fact, the UI Base Wage File (upon which UI benefits are based) includes these reported tips, cash or otherwise, as part of a worker's base earnings.

¹ There are few legislative definitions of “earnings”. However, the Code of Civil Procedure defines “earnings” as “compensation payable by an employer to an employee for personal services performed by such employee...”

At the same time, Labor Code Section 351 provides the following, which is intended to prevent employers from taking any portion of an employee's received tips, or from
ue to tips received:

"No employer or agent shall collect, take, or receive any gratuity or a part thereof that is paid, given to, or left for an employee by a patron, or deduct any amount from wages due an employee on account of a gratuity, or require an employee to credit the amount, or any part thereof, of a gratuity against and as part of the wages due the employee from the employer. Every gratuity is hereby declared to be the sole property of the employee or employees to whom it was paid, given, or left for. . . ."

Since 1994, the Panel has allowed the use of commissions and tips to supplement trainee wages in order to meet the ETP minimum wage requirements. Specifically:

- The Panel may consider the dollar amount of an employer-paid commission earned by an employee when calculating trainee wages. Commissions earned by an employee in lieu of, or supplemental to a regular wage may be used to meet the minimum wage requirement. In such cases, the employer-paid commission, plus hourly wage if any, earned by the employee must be equivalent to, or more than the ETP minimum wage.
- The total dollar amount of cash tips plus the employee's base wage must meet the ETP hourly minimum wage requirements.

Workers Affected By Tips

Contracts to fund training of employees that typically receive tips as part of their employment have been with hotels and resorts in the service industries. The population of trainees whose wages have been augmented by tips have primarily worked in food services and guest services, in occupations such as: bartender, beverage steward, bus person, cocktail server, food server, bell captain, bell person, concierge, housekeeper, shuttle driver, and valet parker. Types of training funded for these occupations typically have included customer service, continuous improvement, communication skills, teambuilding, business skills, and literacy skills.

There have been few funded ETP projects in which tips have been necessary to bring wages up to ETP's minimum requirement. Since 1995, the Panel has only funded 21 such projects, with approximately 1500 trainees (less than one percent of all trainees in approved contracts during the same time period) whose wages included tips to meet the Panel's wage requirement. On average, in these cases tips have accounted for about 30 percent of the trainees' wages to meet the ETP minimum requirement.

Issues

- Tips are considered wages for the purpose of taxing an employee's earnings. In such cases, actual tips have been received by an employee and then reported to the employer as earned and taxable income. However, there is an important distinction between actual earned tips as wages for taxation purposes, and estimated, unearned tips used to supplement low wages for the purpose of meeting ETP's minimum wage requirements. Unlike employer-paid wages, tips are not guaranteed. Although a trainee might earn enough tips to meet the ETP wage requirement at the end of the 90-day retention period, there is no guarantee of the level of tips that a worker will continue to earn in the future.
- All other factors used to calculate training wages are based on employer contributions (commissions, health benefits, etc.); tips, however, depend upon the generosity of customers served and are not employer paid.
- Allowing tips in the calculation of wages may be contrary to ETP's mission to train workers for secure high wage jobs.
- At the same time, under its Job Creation Category, the Panel now funds Career Ladder projects developed in conjunction with EDD. These projects are intended to provide workers in low-wage jobs with the skills needed to advance to better jobs in industries with career advancement opportunities. Since the ETP wage requirement can be waived for workers in Career Ladder projects, the Panel may want to consider limiting the use of tips as wages strictly to Career Ladder projects where it is likely that projects in the hospitality industry may be pursued.

Options

- 1) Continue to allow the use of tips to supplement trainee wages, in order to meet the ETP minimum requirement;
- 2) Limit the use of tips to supplement trainee wages to Career Ladder Projects; or
- 3) Eliminate the use of tips in meeting the ETP minimum wage requirements.